



March 1989 Monthly Survey

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Surveys of Consumers

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Inflation and Interest Rates Expected to Increase Housing Market Bears Greatest Burden

Index Slips

The Index of Consumer Sentiment was 94.3 in the March 1989 survey, down from 95.4 in February and 97.9 in January. Despite the recent small declines, the March 1989 reading was nearly identical to the March 1988 figure (94.6). Overall, the Index was higher in first quarter of 1989 than in the fourth quarter of 1988 (95.9 versus 93.0).

Among families with incomes of \$40,000 or more, the Index was 100.0 in March, down from 109.6 one month earlier and 104.6 one year earlier.

Leading Indicator Component Posts Small Decline

Both the current and expected components of the Index of Consumer Sentiment posted small declines in the March 1989 survey. The Index of Consumer Expectations, the component of the Index of Leading Indicators, stood at 87.6 in March 1989, down from 88.8 in February, and 89.9 in January.

The small consecutive declines during the first quarter still leaves consumer expectations at a very favorable level. For the first quarter of 1989 taken as a whole, the Index of Consumer Expectations was 88.8, the highest quarterly average recorded since the second quarter of 1986.

The current conditions component of the Index of Consumer Sentiment declined to 104.8 in March from 105.7 in February and 110.3 in January. For the first quarter of 1989, the current conditions component averaged 106.9. Although this was above the 103.4 recorded in the fourth quarter of 1988, it was below the average of 110.3 recorded in the third quarter of 1988.

Expected Inflation Rate Posts Sharp Increase

Consumers expected an annual rate of inflation of 5.6% in the March 1989 survey, up from 4.8% in February. The March increase reversed the entire decline recorded since mid 1988, and returned inflation expectations to the four year high first recorded in June and July of 1988.

While this resurgence in inflation expectations is troublesome, it is yet unclear whether it simply represents an immediate but short-lived reaction to the widely publicized and much larger changes in wholesale prices. Whether this upswing is confirmed in subsequent months will determine its ultimate impact. In any event, whether inflation expectations are now running at the 5% or the 5.5% level, they are significantly higher than the 4.1% recorded one year ago.

Interest Rates Still Top Concern

Interest rate expectations remained very unfavorable in the March 1989 survey. Among all families, 73 percent expected increases in interest rates in March, just below the all-time record of 75 percent recorded in February. Just 5 percent of all families in March expected interest rates to decline during the year ahead.

Rising Mortgage Rates Weaken Home Buying Attitudes

Favorable attitudes toward buying conditions for homes fell to the lowest level recorded in four years. Among all families, 60 percent thought that home buying conditions were favorable in the March 1989 survey, down from 64 percent one month earlier, and 71 percent one year earlier.

The decline in favorable home buying attitudes was due to increasing mortgage interest rates. Among all families in the March 1989 survey, 24 percent complained about high mortgage rates, twice the proportion recorded one month earlier, and nearly three times the level recorded one year earlier. Favorable references to current mortgage rates fell to 17 percent in March, from 20 percent one month earlier and 47 percent one year earlier.

The negative impact of increasing mortgage rates was partially offset by the view that mortgage rates would only increase further, promoting the view it was better to buy in advance of those increases. Among all families, 19 percent mentioned the appeal of borrowing in advance of rising mortgage rates in the March 1989 survey, just below the 20 percent recorded one month earlier, but substantially above the 7 percent recorded one year earlier.

Consumer perceptions of home prices also worsened in the March 1989 survey. Favorable references to current home prices fell to 17 percent in March 1989 from 27 percent one year earlier,

while complaints about high home prices rose to 16 percent, from 11 percent one year earlier. Importantly, few consumers saw advantage in buying in advance of rising home prices in either the March 1989 survey (12 percent) or the March 1988 survey (9 percent).

Vehicle Market: Waiting for Discounts

Attitudes toward buying conditions for vehicles continued on their remarkably stable path. In the March 1989 survey, 61 percent of all families held favorable car buying attitudes. This was the tenth consecutive month that favorable vehicle buying attitudes have remained in the narrow range of 60 to 62 percent.

Unfavorable evaluations of car buying conditions have inched upward over the past few months however, to 31 percent in March 1989 from 27 percent in January. The increase has been due to complaints about higher interest rates on vehicle purchases, rising to 13 percent in March from 7 percent in January. This rather modest increase in complaints about rising interest rates was offset by a similar small increase in references to discounted interest rates offered by vehicle manufacturers, rising to 15 percent in March from 11 percent in January.

The fact that consumer purchases of vehicles in the first part of 1989 has been below the levels recorded in late 1988 does not run counter to the relative stability in vehicle buying attitudes. The question asks consumers to give an assessment of buying conditions during the year ahead. Most consumer expect vehicle manufacturers to continue to offer price and interest rate discounts on a intermittent basis. Thus most consumers have been willing to wait and time their purchases to the availability of discounts. Moreover, it is not the mere availability of discounts, but the size of the discount that now determines these timing decisions.

Household Durables

Attitudes toward buying conditions for furniture, appliances, and home electronic goods remained largely unchanged at favorable levels. Among all families in the March 1989 survey, 72 percent thought that buying conditions for large household durables were favorable, just above the 71 percent recorded both one month and one year earlier. These favorable evaluations continued to be based on the perception that price discounts were available, mentioned by 33 percent in both the March 1989 and 1988 surveys.

Current Finances Soften; Future Prospects Remain Strong

The current financial situation of American households weakened slightly in the March 1989 survey, but on balance remained at favorable levels. Importantly, families continue to view their own financial prospects for the year ahead in favorable terms.

Among all families in the March 1989 survey, 42 percent reported that their financial situation had improved. This was slightly below the 44 percent recorded in both of the prior two months, but above the 39 percent recorded three months earlier.

When asked to explain how the financial situation had changed, the small March decline was traced to price changes rather than income changes. No net change was recorded in references to income trends: while fewer families reported income increases in the March 1989 survey in comparison to the previous month (30, down from 36 percent), it was exactly offset by the fall in the proportion of families that reported income declines (13, down from 18 percent).

Complaints that rising inflation had lowered their living standards were made by 15 percent of all families in the March 1989 survey, up from 12 percent one month earlier, and 8 percent one year earlier. Although this represents a significant rise,

complaints about inflationary drains on family incomes are still quite low in comparison with historical patterns.

Despite these concerns about their current financial situation, consumers continued to view their financial prospects for the year ahead in very favorable terms. Among all families in the March 1989 survey, 40 percent expected their financial situation to improve during the year ahead, unchanged from the February reading. During the current economic expansion, in only five of the past 76 monthly surveys has a higher proportion of families expected their financial situation to improve (the cyclical peak was 44 percent recorded in March 1984). Overall, just 9 percent of all families in the March 1989 survey expected their financial situation to worsen during the year ahead.

Outlook for Economy Viewed Favorably

Consumers continue to view prospects for the general economy in favorable terms. Among all families in the March 1989 survey, 55 percent expected good times in the economy as a whole, just below the 56 percent recorded in the prior two months, and above the 47 percent recorded in March of 1988. The majority of families in March (59 percent) expected the growth of the national economy to remain similar to last year's pace.

Favorable employment prospects continue to be the mainstay of this positive outlook. The majority of families in the March 1989 survey (53 percent) expected the national unemployment rate to remain largely unchanged at its current decade low level during the year ahead. On the margin, however, increases rather than further declines were expected by nearly a three-to-one margin (33 versus 12 percent).

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The March 1989 survey included 501 completed interviews conducted between March 1 and March 28, 1989.